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PROGRESSIVE CONSUMPTION TAX ACT OF 2016

FINANCIAL PRODUCTS AND SERVICES FACT SHEET

The Progressive Consumption Tax (PCT) is meant to tax spending, not savings or earnings. To achieve this, the Progressive Consumption Tax Act (PCTA) contains special rules to ensure that savings and investment income, such as interest income, are not taxed.

Financial products and services are subject to special rules because breaking out savings and investment earnings from the provision of services is often difficult in practice.

Take the example of a bank loan. Banks incur labor and other costs in originating and servicing loans and working out bad debt. Some of these costs can be recovered through separately stated charges – for instance, a loan servicing fee. However, banks operating under a consumption tax would have the incentive to recover these costs as a component of the interest rate charged on the loan. Because the cost would be "hidden" in the interest rate—and thus the investment income earned on the loan—the bank would not have to charge tax on its loan servicing and administration services.

Another example is a savings account. As with servicing loans, banks incur labor and other costs in administering a customer's account. Banks operating under a consumption tax could recover these costs simply by allowing the customer's account to earn a lower interest rate.

The same could be said for "free" services that the bank provides. For instance, the cost of issuing "free" paper checks to accountholders can be recovered by lowering the interest rate that the account earns. Because the cost of the "free" paper checks is not charged to the customer, but is instead hidden in the lower interest rate, banks would not have to charge tax on the provision of the paper checks to the customer.

Below is further information on how the PCTA treats financial products and services, along with specific open issues.

General Treatment of Financial Products and Services

The PCTA defines a very narrow category of "financial supplies" that are exempt from PCT. These categories are based on experiences with the implementation of modern goods and services taxes, such as those in Australia and New Zealand. All other financial-related products and services that do not fall into these categories are subject to the PCT. For instance, if a bank offers an account holder paper checks, the bank must charge PCT on the cost of those checks to the account holder.

2016 Update: Financial Products and Services Refinements

The latest version of the PCTA contains several refinements related to financial products and services. These changes are based on the experiences of practitioners from other countries with modern goods and services taxes, as well as suggestions from U.S. stakeholders.

Partial credits for certain inputs related to financial supplies

In particular, the updated PCTA contains a regime similar to the "reduced input tax credit" regime in Australia's GST system. This approach is intended to counteract a problem called "self-supply bias."

As noted above, the PCTA defines a very narrow category of "financial supplies" that are exempt from PCT. Because no input tax credits are available for purchases of goods and services related to making exempt financial supplies, businesses making financial supplies have more incentive to move those goods and services "in house." In other words, instead of contracting with a separate company to purchase, say, online account maintenance, financial institutions would have an incentive to use their employees to provide this service. Among other things, the self-supply bias creates three distortions:

- *Enforceability.* Self-supply makes it harder to distinguish between non-taxable savings and investment income and implicit fees embedded in exempt financial supplies.

- *Small business concerns.* Small businesses that don't have the scale to insource, or businesses that rely heavily on independent brokers rather than in house employees already, are at a disadvantage compared to those who do.

- *Reliance on non-resident providers.* Because they will not be able to claim input tax credits in the U.S., financial institutions may be tempted to acquire services performed outside of the U.S., not subject to the PCT. This will decrease the PCT amount that they pay and make in-country service providers less competitive.

The updated PCTA opts to fix the self-supply bias using the solution devised by the Australian government in the early 2000s. Specifically, the Act provides reduced input tax credits for certain inputs (i.e., purchases of goods and services) related to the provision of financial supplies. By allowing financial services companies and banks to claim partial input tax credits for these inputs, there is less incentive to move the inputs in house; small businesses that must outsource these inputs are not disadvantaged; and there is less of an incentive to use offshore inputs.

Ancillary financial supplies

Sometimes, businesses provide some small financial services to their customers, but providing financial services is not their main business. For example, a repair shop might extend lines of credit to certain customers, though its main business is providing repair services.

To lower the administrative burden for these businesses, which would otherwise have to separately account for their exempt financial supplies (and the purchases relating to those supplies), businesses who do not reach a certain threshold with respect to financial supplies and financial supply purchases are entitled under this draft of the PCTA to a full credit for all of their purchases. This threshold would, however, require businesses that provide ancillary financial supplies to do some separate tracking to ensure that they do not exceed the threshold.

What still needs to be done?

The application of consumption taxes to the financial services sector is difficult. Further feedback from stakeholders is needed to ensure that complicated financial transactions are taxed appropriately.

Specific issues raised by financial products and services are detailed in our Additional Input document. While other countries have experiences with these issues that are very helpful to draw from, we anticipate that the U.S. financial services industry will have unique challenges that will need to be considered and addressed.

How do I submit a comment on the PCTA's application to financial products and services?

Comments on all aspects of the PCTA, including the financial products and services section, are welcome. If you have a suggestion on the Progressive Consumption Tax Act, or more questions, please email PCT@cardin.senate.gov.

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PROGRESSIVE CONSUMPTION TAX ACT OF 2016

FREQUENTLY ASKED QUESTIONS

What is a consumption tax?

A consumption tax is a tax that is imposed on goods, services, and other items sold, exchanged, or consumed. Unlike income taxes, which are imposed on earnings (including savings), consumption taxes are imposed on consuming. Consumption taxes can come in many forms. The most common forms are "indirect" taxes like a retail sales tax or a value added tax.

What is a goods and services tax or value added tax?

A goods and services tax (GST) or value added tax (VAT) is a type of consumption tax that is collected on the amount by which the value of an article has been increased, or the "value added," at each stage of its production or distribution. Thus, from the perspective of a consumer, a GST or VAT is like a sales tax levied on a good or service. But, from the perspective of a business, it is a tax only on the value added to a product or service by that business.

How are value added consumption taxes levied and collected?

The most common method for implementing a value added tax is called the "credit-invoice" system or method. The Progressive Consumption Tax Act (PCTA) uses this system. Under a credit-invoice system, businesses collect consumption taxes imposed on the goods and services that they sell or distribute on a transaction-by-transaction basis. These businesses can also claim a credit for the consumption tax they previously paid on inputs—the business purchases they used to produce or distribute their own goods and services. Total credits are netted against total consumption taxes collected and remitted.

A common alternative to the credit-invoice method is a "subtraction method" consumption tax. Typically, the subtraction system uses businesses' accounting records to calculate value added, and imposes a consumption tax on that amount.

How many other countries have value added consumption taxes?

Approximately 150 countries worldwide have some form of a GST or VAT. Except for the United States, all countries that are members of the Organisation for Economic Cooperation and Development (OECD)—countries with advanced economies similar to that of the United

States—have a consumption tax. Nearly all of the OECD countries use a "credit invoice" method value added tax. For countries seeking admittance to the European Union (EU), the adoption of a value added tax is a prerequisite for membership, due partly to the trade benefits that a GST or VAT provides.

Much has been made of the fact that the United States currently has the highest statutory corporate rate of all the OECD countries. However, this analysis does not take into account the fact these countries also impose a GST or VAT. Below is a table that compares current U.S. tax rates, OECD country averages, and rates imposed under the PCTA.

Country	Top marginal individual income tax rate, 2015	Top marginal corporate income tax rate, 2016	General consumption tax rate, 2016
United States (current)	39.6%	35%	0%
OECD average (unweighted)	36%	23%	19.2%
United States under PCTA	28%	17%	10%

Source: Latest data from OECD Tax Database, available at http://www.oecd.org/tax/tax-policy/tax-database.htm. The latest individual income tax data from the OECD Tax Database for all OECD countries is from 2015.

What are the typical policy critiques of consumption taxes?
While technical critiques of different consumption taxes vary across systems, consumption taxes face two main policy critiques:

Regressivity. Consumption tax systems are often considered to be inherently regressive since low- to middle-income households spend a greater percentage of their income than high-income households do, and so a consumption tax hits them harder. The Progressive Consumption Tax Act counters this directly with significant income tax exemptions, called "family allowances," and Progressive Consumption Tax (PCT) rebates based on income.

Open Spigot. Consumption taxes are often criticized for allowing governments to raise money too easily and without adequate transparency. For those who have this concern, enacting a consumption tax could mean enacting a new and easy-to-adjust lever to raise taxes irresponsibly. The Progressive Consumption Tax Act addresses this concern with a circuit breaker that returns overages from the PCT to taxpayers when revenues exceed predetermined levels.

How does a consumption tax affect savings?
Income taxes have a discouraging effect on savings because they are levied on all taxable income, including savings. Consumption taxes do not tax earnings, including savings. Instead,

consumption taxes focus on spending. If an individual or household spends less, they pay less tax.

Consumption taxes are considered “temporally efficient.” This means that a consumption tax does not affect families’ choices between current and future consumption, since savings are not taxed. Taxing interest, dividends, and capital gains, as under income tax, results in less investment and savings.

How does a consumption tax affect economic growth?

According to both economic theory and recent research on OECD countries’ value added taxes, income taxes are associated with slower long-term economic growth than taxes on consumption.

Recent research on OECD countries’ value added taxes indicate that consumption taxes are associated with greater growth of Gross Domestic Product (GDP) per capita compared to income taxes. In a study that examined 35 years of data on 21 OECD countries, consumption taxes are found to be more growth-friendly than both personal income taxes and corporate income taxes. Corporate income taxes, especially, appear to have the most negative effect on GDP per capita. This evidence suggests that growth-oriented tax reform should move away from income tax revenues and towards consumption tax revenues, as the PCTA does.

In theory, because income taxes levy a tax against savings, taxpayers will choose to do less saving and more current consumption. This arguably results not only in less investment but also less economic growth and lower future living standards, since future consumption is reduced both by the extra current consumption caused by the tax on savings and by the foregone returns that greater savings would have produced.

Who supports consumption-based tax reform?

While preferences on consumption-based tax reform will vary from proposal to proposal, in general, consumption taxes have been historically favored by many policymakers, economists, and others—ranging from Alexander Hamilton (who wrote in Federalist No. 21 on the advantages of consumption taxes) to Bill Gates (who has spoken in favor of a progressive consumption tax). In addition, since the original introduction of the PCTA in 2014, many policymakers, including in Congress, have become increasingly interested in moving to a border-adjustable consumption tax base.

Development of the Progressive Consumption Tax Act

Why introduce the PCTA now?

The PCTA was introduced in the 113th Congress to give legislators, policymakers, and all taxpayers an opportunity to see what this type of tax reform would look like. While consumption taxes are already imposed by all other OECD countries, the PCT would be new to the U.S. tax code.

After a period of considering comments from stakeholders and analyzing its revenue impacts, the Progressive Consumption Tax Act was reintroduced, with several refinements, in the 114th Congress.

Further review and input from stakeholders is needed on the bill. This input is more important than ever as Congress considers moving forward with tax reform—and may consider moving forward with consumption tax proposals. If you have a suggestion on the Progressive Consumption Tax Act, or more questions, please email PCT@cardin.senate.gov.

Have other consumption tax proposals been introduced or discussed in comprehensive tax reform debates?
Other than the PCTA, no consumption tax legislation has been formally introduced in recent Congresses.

However, consumption taxes have long been considered as an option in the comprehensive tax reform debate. National sales taxes have from time to time been considered in Congress since as far back as 1862; special panels, task forces, and Administration reports have included VAT-related recommendations for the past four decades.

Previously introduced consumption-based tax proposals include the "USA Tax" (providing an unlimited deduction for savings, and replacing the corporate income tax with an 11 percent value added tax), the "FairTax" (a national sales tax first proposed in Congress in 1999) and the "X Tax" (a two-part tax that taxes businesses through a subtraction method VAT and taxes individual wage income progressively). The President's Advisory Panel on Tax Reform, formed in 2005 under former President George W. Bush, recommended a partial replacement VAT combined with reductions in the individual and corporate income tax rates. The Panel also considered and enumerated the benefits of a progressive consumption tax plan.

In addition, two 2016 proposals from Members of the House Ways and Means Committee are based on consumption tax principles.

In June 2016, House Ways and Means Republicans released a document entitled "A Better Way for Tax Reform." This plan, also called the "House GOP Blueprint," is not formal legislation, but a white paper detailing the challenges presented by tax reform, the opportunities presented by tax reform, and the high-level structure of a plan for individual income tax simplification and a cash-flow based business tax. While careful to point out that "[t]his Blueprint does not include a value-added tax," the Blueprint does anticipate that eventual legislative text will include major aspects of a subtraction method VAT, including immediate expensing of certain purchases and border adjustability, and notes that these changes "reflect a consumption-based tax."

In July 2016, Representative Jim Renacci (R-Ohio) released a white paper on a proposal called the "Simplify America's Tax System" plan, or SATS. Rep. Renacci's plan reforms the individual income tax code and replaces the corporate income tax with a credit-invoice method value added tax.

Is the PCTA based on of any other country's consumption tax system?
The PCTA is generally based the modern goods and services taxes (GSTs) employed by Australia, New Zealand, and Canada. While all OECD countries have some kind of VAT, the Australia, New Zealand, and Canada GSTs are considered by commentators to be the most efficient to administer, and the Canadian system provides a model on how a federal VAT can interact with sub-jurisdictions (in Canada's case, its provinces) that already impose a sales tax.

That being said, there are several aspects of the PCTA that are unique, such as the way the PCT revenues are used to maintain progressivity and lower income taxes, and how progressivity is maintained through the use of rebates as opposed to select exemptions or preferential rates in the current income tax code.

Why does the PCTA use the "credit invoice" method instead of a "subtraction" or "cash-flow" based method of collection?

The design of the PCTA was carefully considered before it was first introduced in 2014. A critical component of this decision was the collection method. As noted above, the two most common design choices in this respect are the "credit invoice" method and the "subtraction" method. The credit invoice method has been the preferred method of countries that impose consumption taxes and have economies similar to the U.S. The PCTA uses the credit invoice method for many reasons; several major reasons are outlined below.

First, the credit invoice method makes the PCT transparent and more easily enforceable. Under the PCT, there is required reporting of PCT liability on invoices that are generated by each business in a good or service's supply chain. All participants in a supply chain need to undertake this reporting in order for those participants to receive offsetting credits. Hence, there is an incentive for businesses to report correctly to each other and to consumers in order to make sure they don't overpay the government. Under a subtraction method system, entities reports a single, aggregated tax liability, without itemization by transaction. The tax is assumed to be passed onto consumers, but consumers don't get to view a separate statement of the tax embedded in their purchases.

Second, the credit invoice method makes the PCT a more stable, reliable source of reasonable revenue because it is transaction-based and ultimately imposed on individual consumers, not businesses. Therefore, it is typically considered less apt to draw political pressure for preferential tax treatment by businesses, industries, and sectors providing certain goods or services. In addition, because the tax has to be stated on invoices (like state and local sales taxes) to consumers, the effect of any proposals to raise the PCT would be highly visible to taxpayers.

Third, using the credit-invoice method means the PCT is compliant with existing WTO rules. While there are arguments that a subtraction method VAT is economically equivalent to a credit invoice method and thus should also be considered WTO compliant, no such scenario has ever been evaluated in the WTO. A subtraction method VAT, or a variation of a subtraction method VAT, may result in litigation in the WTO and create considerable uncertainty for businesses subject to that tax system.

Finally, paying taxes on a transactional basis under the credit invoice method means the PCT can become more and more automated as technology improves. As we move away from a cash economy, for instance, payment at the cash register (or Internet website) could be translated to immediate remittance of tax to the government, greatly lowering the tax gap. The same can't be said for subtraction method consumption taxes, which are not collected on a transaction-by-transaction basis.

What changes have been made to the PCTA since it was first introduced in 2014?
The updated PCTA contains several refinements to how financial products and services are taxed. These refinements are based on the input we received thus far from stakeholders and conversations with practitioners familiar with modern goods and services taxation systems. Further details on these changes can be found on our Financial Products and Services Fact Sheet and Additional Input document.

In addition, the updated PCTA contains an exemption for small businesses with annual receipts under $100,000. This exemption level is based on levels in countries with developed economies similar to the U.S. Further feedback from the small business community on establishing a specific exemption and its level is welcome.

What are the revenue impacts of the PCTA?
The full budgetary and distributional impact of the PCTA have not been evaluated by the Joint Committee on Taxation. While the rates in the PCTA have been based on a comparison of U.S. tax liabilities to OECD countries with value added taxes, and a similar plan estimated by the Tax Policy Center, depending on the feedback we receive and other changes to the PCTA, these rates and their structure may change.

However, since its release in 2014, the PCTA's static and dynamic revenue effects have been analyzed by the Tax Foundation. That analysis can be found here. According to the Tax Foundation's Taxes and Growth model, the PCTA would be pro-growth and progressive on both a static and dynamic basis; however, a 14.2 percent PCT rate, rather than a 10 percent rate, would be needed to achieve revenue neutrality on a static basis.

What issues still need to be addressed?
As reintroduced in the 114th Congress, the updated Progressive Consumption Tax Act is meant to provide an opening for further discussion and a continued opportunity to review legislative language for this type of comprehensive tax reform. Overall, the Act shows how a PCT can make our tax code fair and more effective. However, there are open issues that the Act does not address in its current form. More details on open issues can be found in our Additional Input document.

How can I submit a comment?
If you have a suggestion on the Progressive Consumption Tax Act, or more questions, please email PCT@cardin.senate.gov.

Details on the Progressive Consumption Tax (PCT)

What is the PCT rate set in the PCTA?
As introduced, the PCTA sets the PCT rate at 10 percent.

It is important to keep in mind that the full budgetary and distributional impact of the PCTA has not been evaluated by the Joint Committee on Taxation. Since the U.S. is a low-tax country compared to other advanced-economy countries, the PCT will likely be set at a rate below the current OECD average of approximately 19 percent. A score by the Tax Policy Center of a similar plan by Professor Michael Graetz resulted in a revenue-neutral rate of 12.9 percent, and a report by the Tax Foundation shows that the PCTA is pro-growth and progressive on a static and dynamic basis, but that revenue neutrality on a static basis will require a PCT rate of approximately 14 percent. Depending on the Joint Committee on Taxation analysis, the feedback we receive, and any further changes to the PCTA, the rates and their structure under the current bill may change.

What transactions are subject to the PCT?
The PCT is a very broad-based consumption tax. Thus, almost all goods, services, and other items, unless exempt or zero-rated under the Act, will be subject to the PCT.

Specifically, goods, services, and other items (called “supplies”) are taxable if: (1) the supply is made for consideration; (2) the supply is made in the course of carrying on a trade or business or other type of commercial activity; and (3) the supply is made in connection with the United States.

Other types of commercial activities subject to the PCT include the commercial activities of nonprofits and governments, which will also be required to comply with the provisions of the PCT.

What transactions are not subject to the PCT?
As introduced, there are three types of transactions under the PCT. Taxable transactions include almost all goods, services, and other items. However, there are two additional, narrow classes of supplies that are subject to special rules.

(1) PCT is not levied on “exempt” supplies. There are only four types of exempt supplies: the provision of financial supplies, residential housing, residential rent, and de minimis supplies. Financial products and services are subject to special considerations. In addition, certain small businesses are exempt from the PCT regime.

(2) PCT is payable at a rate of 0 percent on “zero-rated” supplies. The only zero-rated supplies are exports or use of goods, services, and other items (such as rights) outside of the United States.

What is the difference between “exempt” and “zero-rated” transactions?
If a supply is exempt, no PCT is levied on that supply. However, no input tax credits related to that supply may be claimed by the business providing the exempt good or service.

If a supply is zero-rated, a business may still claim input tax credits for the business inputs used to make the zero-rated supply.

How is the PCT collected on transactions subject to the PCT?
The PCT is a credit invoice consumption tax. Under the credit invoice method, businesses collect PCT on taxable goods and services that they provide to either another business or consumer on a transaction-by-transaction basis. These business are then allowed to reduce the amount of PCT they are liable to remit by a credit equal to the amount of PCT they have previously paid to other businesses in purchasing inputs (such as intermediate goods, services, and equipment).

Are there any other special rules that apply to exempt financial products?
A very narrow class of financial products is exempt from the PCT. This narrow class is drawn from the experiences of existing consumption tax systems like those in Australia and New Zealand. Exempt financial products and services include the provision of a bank account, a debit or credit arrangement, a mortgage, a superannuation fund, an annuity, insurance, a financial guarantee, an indemnity, currency, securities, or derivatives. Any products or services related to but separate from the provision of these products—e.g., checks provided along with a bank account—must be separately stated and the PCT must be charged for those products or services.

The latest version of the PCTA contains several refinements related to financial products and services. These changes are based on the experiences of practitioners from other countries with modern goods and services taxes, as well as suggestions from U.S. stakeholders.

In particular, the updated PCTA contains changes similar to the “reduced input tax credit” and “financial acquisitions threshold” regime in Australia’s GST system. More details on this system and areas for further consideration can be found in our Financial Products and Services Fact Sheet and Additional Input document.

Who pays the PCT?
The PCT is a consumption tax, and so is ultimately paid by the consumer. However, sellers are required to collect and remit the tax on goods and services they provide. Sellers include not only businesses, but also nonprofits and governments to the extent they engage in taxable transactions.

In certain cases, special collection rules provide that the purchaser, rather than the seller, remit the tax. These special rules apply to imports of goods generally, and imports of services and other items to businesses. The PCT for imported goods is intended to be collected at the border, much like a customs duty. Thus, the importer is liable for the tax. In addition, "reverse charge" rules apply to certain services and other items performed or done outside of the United States, but used within the United States in a trade or business. In these cases, the purchasing business must remit the tax.

How would a typical consumer see or pay the PCT?
To a typical consumer, the PCT would be paid just like a sales tax and would replace their income tax liability. Low- and middle-income consumers would receive additional rebates to further offset the burden of the PCT. For a purchase, a retailer would charge the consumer PCT at the register (or website). PCT would be stated on the receipt the consumer receives.

Do private consumers need to keep track of PCT charged on their purchases?
No, in general, private consumers—end-users of goods and services—do not need to keep track of PCT charged on their purchases. Under the PCTA, PCT is typically collected and remitted by sellers. Private consumers also do not need to keep track of their PCT liability in order to claim the rebate, which is based on earned income or adjusted gross income.

Is there an exemption for small businesses?
Yes. The updated version of the PCTA exempts small businesses with under $100,000 in annual receipts from collecting the tax. Exempt businesses may nonetheless collect the PCT if they prefer. This exemption level is based on levels in countries with developed economies similar to the U.S. Further feedback from the small business community on establishing a specific exemption and its level is welcome.

How is the PCT progressive?
The PCTA has two measures that counteract the regressivity inherent in consumption taxes. The first is the large income tax exemption, called a "family allowance," of $100,000 for joint filers, $50,000 for single filers, and $75,000 for head of household filers.

The second is a PCT rebate designed to counteract the new consumption tax burden and make up for the loss of the Earned Income Tax Credit (EITC), the Child Tax Credit (CTC), and the Additional Child Tax Credit (ACTC). Since the goal is to make the new tax system that includes the PCT as progressive as the current system, these programs aimed at low- and moderate-income families need to be replaced. Therefore, the PCT includes a rebate that replaces each of these components. Individuals and families that do not have an income tax liability would still be able to receive rebates.

More details on the calculation and administration of the rebate are contained in our Progressivity Fact Sheet.

Details on income tax reforms

What are the new income tax exemptions and rates?
The PCTA provides a significant individual income tax exemption, called a "family allowance," of $100,000 for joint filers, $50,000 for single filers, and $75,000 for head of household filers. The personal exemption for 2017 is $4,050 and the standard deduction is $12,700 for joint filers, $6,350 for single filers, and $9,350 for head of household filers.

For those who still have an individual income tax liability, there will be three marginal brackets, set at 15, 25, and 28 percent, with the following thresholds:

Taxable Income		Marginal Rate
Over	But Not Over	
Single		
$0	$50,000	15%
$50,000	$250,000	25%
$250,000		28%
Married Filing Jointly		
$0	$100,000	15%
$100,000	$500,000	25%
$500,000		28%
Head of Household		
$0	$50,000	15%
$50,000	$250,000	25%
$250,000		28%

Under current law, there are seven marginal brackets, with a top marginal rate of 39.6 percent that in 2017 applies to taxable income over $418,400 for single filers, $470,700 for joint filers, and $444,500 for head of household filers.

In this version of the PCTA, the corporate income tax rate is lowered to 17 percent. The top statutory corporate tax rate in the U.S. is currently 35 percent.

How else does the individual income tax change?
The PCTA simplifies the individual income tax. Because an income tax liability is eliminated for most households, many individual income tax preferences are streamlined or removed.

Four major tax benefits are retained: (1) the charitable deduction; (2) the state and local tax deduction; (3) health and retirement benefits; and (4) the mortgage interest deduction.

Individual income tax deductions for alimony payments, investment interest, and gambling losses are also retained because alimony received, investment income, and gambling winnings are included in income under current law. Including these deductions is necessary to prevent the duplicative taxation of alimony payments and to properly measure the net income from gambling and investment.

The foreign tax credit is retained for income taxes paid to a foreign government on income earned outside the U.S. Finally, the individual alternative minimum tax (AMT) would be repealed.

How else does the corporate income tax change?
Aside from the tentative rate change mentioned above, the corporate AMT is repealed in its entirety.

What happens to credits like the EITC?
Because the significant family allowances provided by the PCTA eliminate an income tax liability for most households, the benefits currently provided through refundable income tax credits like the EITC are instead provided through a rebate. For more information on the rebate, please see our Progressivity Fact Sheet.

How does the PCTA interact with other tax reform proposals?
The PCTA makes many changes to the individual income tax. However, as introduced, the PCTA is not meant to foreclose consideration of other corporate income tax reform proposals. Instead, it is intended to add another important proposal to the tax reform debate.

However, comments on the PCTA that will receive the most consideration will be those on the reforms specifically proposed by the PCTA. We do not anticipate making large changes to, for example, corporate international taxation within the current PCTA framework itself.

Details on the Revenue “Circuit Breaker”

Why include a revenue “circuit breaker”?
A major criticism of consumption taxes is based on the concern that the government will become “addicted” to consumption tax revenue. For those who have this concern, enacting a consumption tax means enacting a new and easy-to-adjust lever to raise taxes irresponsibly and without much transparency.

One goal of PCT-based reform is to more reliably raise the revenues that we need to for real investments that benefit all taxpayers—such as investments in defense, health, education, and infrastructure programs. However, the PCT is not meant to be a means to quickly raise revenues while disregarding the effects of higher consumption taxes on U.S. families and employers. Thus, the PCT includes the revenue “circuit breaker” mechanism to address these concerns and to benefit taxpayers.

How does the revenue "circuit breaker" work?
The revenue "circuit breaker" puts cash back into taxpayers' pockets if PCT revenue in a given year exceeds a certain threshold.

Specifically, under this version of the PCTA, if PCT revenues as a percentage of GDP exceed 10 percent over the calendar year, then any excess revenue will be returned to all individual income tax filers, including those taxpayers who have filed for a PCT rebate. As introduced in the 114th Congress, the Progressive Consumption Tax Act returns a flat rebate to single and head of household filers, doubles that rebate for joint filers, and includes additional rebate money for filers with dependents.

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PROGRESSIVE CONSUMPTION TAX ACT OF 2016
ADDITIONAL INPUT

All comments on the Progressive Consumption Tax Act (PCTA) are welcome. Insights and concerns raised by stakeholders over the past Congress—from both individuals and businesses—have been very helpful and appreciated. Further input and discussion are crucial, especially as Congress considers moving forward with comprehensive tax reform. In addition to general comments on the Act, we are interested in feedback on the issues outlined in this document.

If you have any suggestions on the Progressive Consumption Tax Act, or more questions, please email PCT@cardin.senate.gov.

Transition and state and local harmonization

We are continuing to examine several high-level, structural open issues. The biggest of these issues relate to a transition from our current system to the proposed PCTA system. Specific transition issues include: the PCTA's effective date (set now at January 1, 2018); how transactions spanning the effective date should be treated; issues related to large consumer durable goods like motor vehicles and housing; and making the transition fairer for older taxpayers.

Another significant issue is how the PCT as proposed will interact with state and local sales taxes. Resolving this important issue will require discussion with state governments. While Canada's Harmonized Sales Tax (HST) can act as a model, we recognize that the U.S. system poses unique considerations and challenges. Aside from sales tax issues, many states base their income tax systems on the federal system. As with any federal income tax overhaul, this interaction must be carefully considered.

Any comments, concerns, and potential solutions regarding these two critically important issues are welcome.

Financial services issues

The updated PCTA contains several refinements related to the treatment of financial products and services. However, given the complexities that arise when taxing financial products and services under a consumption tax system, more input is needed.

Issues related to the reduced credit system

The PCTA provides a partial credit, similar to Australia's reduced input tax credit system, for PCT paid on certain goods and services purchased by businesses to provide financial supplies. This system is meant to counteract "self-supply" bias, discussed in more detail in our Financial Products and Services Fact Sheet.

The list of goods and services included in the legislation represent a summary of those that were identified as particularly susceptible to self-supply under the Australian regime. Input on whether to add to, delete from, or refine this list would be helpful. Moreover, the Australian regime provides quite a bit of regulatory authority to adjust the rate of the reduced credit and what type of goods and services qualify. Input on the flexibility needed in this regard would also be appreciated.

In addition, the system provided for in this version of the PCTA is not the only way to address self-supply bias. For instance, instead of providing a partial credit only with respect to the purchase of goods and services that are easy to move in-house, all purchases related to exempt financial supplies could be subject to a lower partial credit.

Another alternative is utilized in New Zealand, which allows, on an elective basis, zero-rating of financial supplies to taxable customers. Electing companies can zero rate (claim full input tax credits, but charge no consumption tax) to customers, but only if those customers are taxable businesses (defined as customers having themselves 75% taxable sales).

Feedback regarding the partial credit system in the updated PCTA and these other options is welcome as we further refine the draft going forward.

Ancillary financial supplies

As noted in our Financial Products and Services Fact Sheet, sometimes, businesses provide financial services to their customers, but providing financial services is not their main business. For example, a repair shop might extend lines of credit to certain customers, though its main business is providing repair services.

To lower the administrative burden for these businesses, which would otherwise have to separately account for their exempt financial supplies (and the purchases relating to those supplies), the PCTA provides that businesses that do not reach a certain threshold with respect to financial supplies and financial supply purchases are entitled to a full credit for all of their purchases. This threshold would, however, require businesses that provide ancillary financial supplies to do some separate tracking to ensure that they do not exceed the threshold.

Comments or suggestions are welcome on these or other proposals for businesses that supply an ancillary amount of financial supplies compared to their total business activity. We are particularly interested in comments regarding the level of the threshold and views on the administrative challenges the threshold poses along with potential solutions to those challenges.

Select administration issues

Aside from transition issues, more input is needed regarding the administration and implementation of the PCT, the rebate provided to maintain progressivity, and the circuit breaker rebate. Comments on all of these issues are welcome. Specific items include:

Reporting periods. The PCT provides several rules for reporting liability and claiming credits. Comments on the timing of filings for both large and small businesses, the information provided on invoices, and other reporting items would be helpful. Sharing experiences with and best practices of state sales tax systems, which can contain similar requirements, would also be helpful.

Registration system. To ensure the efficient implementation of the PCT, including the remittance of tax and the claiming of credits by taxable businesses, more input is needed on best practices regarding a PCT registration system. Any experiences internationally or with state and local sales tax registrations would be particularly helpful.

Apportionment and bundling. One of the goals of the PCT is to correctly measure the tax liability and credits related to taxable, zero-rate, and exempt items, but still keep administrative costs as low as possible. Suggestions regarding apportionment rules, rules regarding the bundling of transactions, and rules on incidental supplies are welcome.

Progressive rebate administration. Currently, the rebate provided to offset the burden of the PCT for low- and middle-income families is meant to be issued before purchases are made, in order to prevent rebate-receivers from paying PCT out-of-pocket. To avoid any complications related to "clawing back" rebates, the rebate will be issued based on prior year informationAny suggestions regarding the timing of the rebate, its calculation, the information required, and its distribution are welcome.

Transactions with non-resident businesses. Input on best practices regarding cross-border transactions between non-resident businesses and U.S. businesses would also be appreciated. The PCT is meant to encompass a broad range of goods and services that are used or consumed in the U.S. However, we understand that administrative and other challenges can arise with respect to transactions involving non-resident businesses and supplies like intangibles, including digital products and services.

PROGRESSIVE CONSUMPTION TAX ACT OF 2016
SECTION-BY-SECTION

TITLE I: PROGRESSIVE CONSUMPTION TAX

Title I of the Progressive Consumption Tax Act (PCTA) creates a new chapter 30 in the Internal Revenue Code. Chapter 30 contains all provisions related to the Progressive Consumption Tax (PCT), including the imposition of the PCT, the definition of a taxable supply, providing for input credits, outlining administrative rules, and defining other terms.

Subchapter A. Subchapter A contains rules on the imposition of the PCT.

Section 3901. Section 3901 imposes a tax on each "taxable supply" at a rate of 10 percent of the "taxable amount." Section 3901 also "zero rates" goods, services, and other items exported out of the United States.

- Exported goods and services are zero-rated because the PCT is meant to capture consumption within the United States. Thus, when a good is exported out of the United States or a service or other item is used outside of United States, the rate of the PCT is zero. Under this version of the Progression Consumption Tax Act, goods must be exported from the United States within 90 days of the provider (the seller) providing an invoice for the supply. Requirements regarding invoices are outlined in section 3922.

Section 3902. Section 3902 defines the "taxable amount" – the amount on which the 10 percent PCT is imposed.

- Where money is the only consideration provided, the taxable amount is the price charged by the person supplying the good, service, or other taxable supply, plus all charges for transportation and other items (for example, insurance charges) payable to the supplier.

  The taxable amount does *not* include the PCT or state and local sales taxes.

- Where money is *not* the only consideration provided, the taxable amount is the fair market value of any non-monetary consideration plus the amount of money paid. For example, when a customer pays a seller with both money and goods, the taxable amount equals the money plus the fair market value of the goods. Transportation and other items payable to the provider are included in the taxable amount.

- For imports, the taxable amount is the customs value plus any duties imposed. The customs value includes invoiced charges for transportation and other items payable to the importer.

Section 3902 also contains a special rule for sales of used goods. The purpose of this rule is to balance the economic impact of the tax on a supply of a previously untaxed used good that is later sold and taxed.

Subchapter B. Subchapter B contains rules regarding which sales, exchanges, or other transactions, called "supplies," are taxable.

Section 3911. Section 3911 defines "taxable supply".

Under *Section 3911(a)*, taxable supplies come in two general categories.

- First, any property imported into the United States is a taxable supply. Since the PCT is meant to be imposed on consumption in the United States, the PCT applies to imports.

- Second, other than imports, a supply is taxable if:

    - the supply is provided by the provider (the seller) in the course of the provider carrying on a trade or business;

    - consideration is provided in return; and

    - the supply is made in connection with the United States.

    Because the PCT is meant to be imposed not only on private sellers or suppliers, but also on nonprofits and the governments when they engage in commercial activity, Section 3911 contains provisions to capture when those entities make "taxable supplies". For example, PCT will be imposed when the government sells a map of a national park, or when a nonprofit museum sells souvenirs at its gift shop. These rules are meant to ensure that private businesses are not at a disadvantage if nonprofits or governments engage in the same commercial activities.

Section 3911(b) defines "supply." "Supply" is a term that is broad and is meant to capture most purchases or transfers of property (real, tangible, and intangible), services, and rights.
However, services provided by an employee for his or her employer are not considered a "supply". Therefore, the salaries and wages earned by the employees and paid by their employers are not taxable.

Section 3912. Taxable supplies must be "made in connection with the United States." Section 3912 defines this phrase.

- A supply of *tangible property* is made in connection with the United States if the property is delivered or made available to the recipient in the United States. This includes property that is assembled in the United States or is eventually physically removed from the United States.

The "assembled in" provision addresses situations where parts of a final good are assembled or installed in the United States. For example, if a U.S. company purchases an aircraft from a company abroad, and that company imports the aircraft parts into the United States and assembles the aircraft in the United States, then the supply of the aircraft is considered made in connection with the United States.

The "removed from" provision is meant to capture supplies of goods that are later taken out of the United States. For example, if a U.S. company makes a sale of goods to a company abroad, and then ships those goods outside of the United States to the company abroad, the supply of the goods is a taxable supply. Note that if the goods are considered exported supplies under section 3901, the goods would be taxed at a zero rate.

- A supply of *real property* is made in connection with the United States if the real property is located in the United States.

- A supply of *anything else (services, intangible property, and other supplies)* is made in the United States if it is used, performed, or done in the United States or if it is provided through a trade or business in the United States.

  This rule for services, intangible property, and other supplies is written broadly in order to make sure that supplies that are consumed in the United States are considered made in connection with the United States.

Section 3913. Section 3913 explicitly exempts four supplies from tax. These include:

- the rental and leasing of residential real property, and the sale of any residential real property not considered new. Property is not considered new if it has been continually rented for five years, but is considered new if substantial renovations have been made to the property after the effective date of the Act.

  The exemptions related to residential real property are meant to lessen the tax burden on housing and to keep taxpayers who are selling their homes from being drawn into the administrative complications of collecting and remitting the PCT on a one-off transaction.

- Financial supplies. This narrow class of financial products and services, defined later in the legislation, are exempted in order to prevent the imposition of the PCT on returns to saving and investment.

- Supplies made by "nonparticipating small suppliers." This provision exempts certain small businesses from the PCT regime. "Nonparticipating small suppliers" are those businesses with aggregate taxable PCT revenues of not more than $100,000 for the immediately preceding four calendar quarters. Small businesses who could be considered "nonparticipating small suppliers" but wish to participate in the PCT regime may elect to do so. The taxable PCT revenues of members of the same controlled group of corporations and all taxpayers under common control are aggregated for purposes of applying the threshold.

- De minimis supplies. These supplies are exempt because the cost of administering the PCT with respect to the supplies is greater than the revenue raised by taxing the supplies. The Secretary of the Treasury makes this determination pursuant to section 3932(b).

<u>Subchapter C.</u> Subchapter C contains rules regarding when providers (sellers) are entitled to input tax credits for the purchases they make in providing their own taxable supplies. Subchapter C thus provides the "credit" piece of the credit-invoice mechanism the PCT employs. Under the credit-invoice system, providers assess the PCT on their taxable supplies (as prescribed by Section 3901). However, providers who make taxable supplies are also permitted to reduce the amount of tax for which they are liable (see Section 3921) by input credits for PCT paid on business inputs (intermediate goods, services, machinery and other equipment, for instance).

Section 3916. Section 3916, the only section in Subchapter C, contains the rules related to these input credits.

- *Section 3916(a)* provides the general rule. Section 3916(a) essentially provides that taxpayers who are required to remit PCT on their taxable supplies can offset their PCT liability by the amount of tax imposed on their "creditable acquisitions" made with respect to their taxable supplies.

  In other words, taxpayers with a PCT liability may claim input tax credits equal to the amount of PCT previously paid with respect to purchases used to make their own taxable supplies. Note that PCT liability and credits are *not* matched for each individual item sold. Rather, aggregate credits are subtracted from aggregate PCT liability. This can result in a net liability or, in some cases, excess credits (see below).

- *Section 3916(b)* defines "creditable acquisitions." In particular, a creditable acquisition of a supply must be subject to PCT and must be for use in the trade or business of the taxpayer claiming the credit. As with the imposition of the PCT, parallel rules are provided to ensure that nonprofits and governments that have a PCT liability will be permitted to also claim input tax credits for their creditable acquisitions.

- *Section 3916(c)* contains two new refinements related to purchases used to make financial supplies.

  - First, this subsection creates a threshold for businesses that only make a small amount of financial supplies ancillary to their main line of business. Businesses that do not reach this threshold, called "qualified small financial suppliers," may claim full credits on the tax remitted on all of their purchases, even if those purchases are subsequently used to make exempt financial supplies. This subsection is intended to relieve businesses that make only a small amount of financial supplies from undertaking the administrative burden of allocating the tax paid on their purchases between their financial supplies and taxable supplies. Specifically, this subsection:

    - Defines "qualified small financial supplier" as a supplier that makes taxable purchases for the purpose of making financial supplies and the credits related to make those purchases does not exceed the lesser of $150,000 or 10 percent of the total amount of credit to which the supplier would be entitled.

    - These calculations are done every month, looking back over a 12 month period.

    - Aggregation rules identical to those used to determine whether a supplier is a "non-participating small supplier" (see section 3913(b)(3)) apply in determining whether a supplier exceeds the amounts above.

  - Second, this subsection creates a partial credit regime for certain purchases used to make financial supplies. Overall, the section is meant to provide a 60 percent partial credit for PCT paid on certain goods and services used by the purchasers of these goods and services to subsequently make exempt financial supplies. The purpose of providing this partial credit is to prevent the "self-supply bias" that can arise when credits are not claimable on inputs related to financial supplies. In particular, this subsection:

    - Provides that purchasers who make "partially creditable acquisitions" are entitled to partial credits at an applicable percentage;

    - Sets the "applicable percentage" at 60 percent; and

    - Defines the list of partially creditable acquisitions. This list of goods and services are considered most susceptible to self-supply bias based on the experiences of other countries with modern goods and services taxes.

- *Section 3916(d)* addresses situations where supplies are used only partly for a creditable purpose (for example, where the taxpayer purchases a computer that is used partly in his or her business, and partly for personal use). Credits are only permitted to the extent the purchased supply is used for a creditable purpose (that is, used in the taxpayer's trade or business, with parallel provisions for nonprofits and governments).

- *Section 3916(e)* addresses situations where a supplier has credits in excess of his or her PCT liability. Where that is the case, the excess credit is treated as an overpayment, and is refunded to the supplier. For example, this will often be the case with suppliers who are primarily exporters. Goods exported from the United States are zero-rated—the goods are taxable supplies, but PCT is imposed at a zero rate, because the exported goods are not consumed in the United States. At the same time, the exporting supplier is allowed to claim input tax credit for his or her purchases used to make the taxable supplies that are exported.

Subchapter D. Subchapter D contains various administrative rules.

Section 3921. Section 3921 makes clear that the supplier of the taxable supply is liable for the tax imposed by section 3901. Because the PCT is a tax on consumption, the incidence of the tax will fall on consumers. However, in general, providers (sellers) will be responsible for collection and remittance of the PCT.

In certain cases, Section 3921 provides that purchasers must themselves remit the PCT.

- First, purchasers must remit the PCT for imported goods. While the details are not explicitly outlined in this version of the Progressive Consumption Tax Act, the PCT for imported goods is meant to be collected at the border, much like current duties and other customs fees.

- Second, in the case of a supply other than a supply of imported goods, purchasers must remit the PCT if the supply is performed or otherwise done outside of the United States but is used in the United States in carrying on a trade or business (with parallel rules for nonprofits and governments).

  Those familiar with other goods and services taxes might recognize this provision as a "reverse charge" rule. Like reverse charge provisions in other countries, section 3912's reverse charge rule is intended to eliminate the advantage of purchasing services that are performed outside of the United States from a provider who is not required to remit PCT. Note that most private consumers will not be responsible for the reverse charge of the PCT, as they will not acquire the imported service for use in a trade or business.

Section 3922. Section 3922 outlines rules for invoices. Tax invoices, specifying the amount of tax paid, are required to be provided by providers of taxable supplies. No credits under section 3916 are permitted without an invoice. For purposes of claiming input credits, the invoice requirement can be waived in certain cases (such as where the taxpayer who is claiming the credit can demonstrate that he or she failed to receive an invoice without fault). Invoices must be furnished within 15 business days after the "tax point" of the supply (defined in section 3923).

Section 3923. Section 3923 contains filing rules. In general, taxpayers liable for the PCT must file a return for each "taxable period." For most taxpayers, a "taxable period" is a calendar quarter. However, businesses who make taxable supplies for any month in excess of $20 million must file monthly.

- PCT liability must be allocated to a taxable period if the taxable supply has a "tax point" within the taxable period. Tax point is defined as the earlier of the time when any income from making the supply is treated as received or accrued by the supplier, or the time when the supplier receives payment for making the supply. The "tax point" of an importation occurs when the property is entered for consumption in the United States.

- Credits are claimable for the taxable period in which the invoice related to the creditable acquisition is received.

Section 3924. Section 3924 allows the Secretary of the Treasury to prescribe regulations regarding the treatment of related businesses under the PCT.

Section 3925. Section 3925 requires the Secretary of the Treasury to submit semi-annual reports on the implementation and administration of the PCT.

Section 3926. Section 3926 requires the Secretary of the Treasury to prescribe regulations necessary to implement and administer the PCT.

Subchapter E. Subchapter E contains several definitions and rules that coordinate the rules of the PCT with certain income tax rules.

Section 3931. Section 3931 defines several terms related to the implementation of the PCT that are consistent with other Internal Revenue Code sections (such as "business," "business day," "person," "employee," and "United States."). Section 3931 also defines two terms specific to the PCT:

- The terms “provide” and “provider,” where used in new chapter 30, are meant to include the importation of property and importers.

- The term “financial supplies” is defined to include a very narrow class of financial products. This term is based on the Australian model of taxing financial supplies, which provides for a similarly narrow list.

Section 3932. Section 3932 contains special rules related to coordination with income tax provisions under subtitle A of the Internal Revenue Code. In particular, if an input tax is permitted with respect to the purchase of a taxable supply, for purposes of income taxes, that credit is treated as a reduction in the amount that the taxpayer paid for the supply. The amount allowable as a deduction for the PCT will be determined without regard to any credit.

Section 3932 also provides rules related to the computation of percentage depletion under Internal Revenue Code section 613, and allows the Secretary of Treasury to issue regulations related to the de minimis provision of taxable supplies.

Finally, Section 3932 provides that the PCT will be applied to supplies provided after December 31, 2017.

TITLE II: INDIVIDUAL AND CORPORATE TAX REFORM

Title II contains changes to the individual and corporate income tax code. On the individual side, Title II provides a significant exemption of $100,000 for joint filers, $50,000 for single filers, and $75,000 for head of household filers. The individual income tax is also simplified for all filers, and rates are reduced. Title II also provides for a rebate, structured as a refundable credit, which, along with the exemption, is intended to ensure that the entire system is at least as progressive as current law. Finally, the corporate rate is reduced.

<u>Subtitle A:</u> Subtitle A contains individual income tax reforms, including reducing rates and consolidating brackets, providing for a large family allowance, and simplifying the individual income tax by streamlining and repealing certain credits and deductions and repealing the alternative minimum tax. Subtitle A also contains a rebate targeted at low- and middle-income families to counteract the regressivity of the PCT.

Individual income tax reforms

Section 201. Section 201 contains individual rate reductions. Instead of the seven marginal brackets under the current system (with a top marginal rate of 39.6 percent), Section 201 prescribes three marginal brackets, set at 15, 25, and 28 percent.

- The 15 percent rate applies to taxable income up to $50,000 for single filers, $100,000 for joint filers, and $50,000 for head of household filers.

- The 25 percent rate applies to taxable income over $50,000 to $250,000 for single filers, over $100,000 to $500,000 for joint filers, and over $50,000 to $250,000 for head of household filers.

- The 28 percent rate applies to taxable income over $500,000 for joint filers, $250,000 for single filers, and $250,000 for head of household filers.

Section 201 also updates the current cost-of-living adjustments to reflect the new rates and the effective date of the rate changes. Adjustments are made for taxable years beginning after December 31, 2018; the new rates come into effect for taxable years after December 31, 2017.

Section 202. Section 202 amends the definition of "taxable income" to reflect the new "family allowance amount." The family allowance amount is $100,000 for joint filers, $50,000 for single filers, and $75,000 for head of household filers. Like, for example, the current standard deduction and personal exemption, the family allowance is subtracted from adjusted gross income (AGI) in order to determine taxable income.

- The family allowance, which is much larger than the standard deduction and personal exemption, is intended to replace the personal exemption for individuals and many of the deductions taken to reduce taxable income under current law (changes detailed later in the legislation). Individuals who have short taxable years will have their family allowance amounts prorated. The family allowance amounts are adjusted for inflation after 2017.

Section 202 also contains many conforming amendments to ensure the tax code reflects the switch to the family allowance for taxpayers whose current filing status, income tax computations, payroll tax withholding amounts, or other tax benefits depend on the taxpayer taking into account a personal exemption or standard deduction.

Section 203. Section 203 repeals the current limitations relating to itemized deductions, known as the PEP and Pease limitations, for tax years beginning after December 31, 2017. Section 203 also contains several conforming amendments related to the repeal of PEP and Pease limitations.

Section 204. Section 204 repeals the preferential treatment for capital gains. Capital gain income that qualified for this treatment is taxed at ordinary rates for tax years starting after December 31, 2017.

Section 205. Section 205 simplifies the income tax by repealing a range of personal, non-business deductions and credits, including tax benefits that are moot due to the family allowance, which eliminates an income tax liability for a broad range of taxpayers.

- The mortgage interest deduction, charitable deduction, deduction for state and local taxes, deduction for gambling losses, deduction for alimony payments, and deduction for investment interest are *not* repealed.

- Business-related tax benefits remain the same. Note that these business-related tax provisions retain incentives for important programs that affect many individual taxpayers, like incentives for employer-provided retirement plans.

- The alternative minimum tax is repealed.

Rebate

Section 206. Section 206 establishes a progressive tax rebate. This rebate, along with the family allowance, is intended to make the new system outlined by the Progressive Consumption Tax Act at least as progressive as under current law.

Specifically, Section 206(a) replaces current Internal Revenue Code Section 32 (the earned income tax credit) with a comprehensive earned income rebate.

- Pursuant to *Section 32(a)*, the new rebate is the sum of three parts: the earned income amount, the child benefit amount, and the additional child benefit amount. "Eligible taxpayers," defined later in the section, may claim the rebate.

- *Sections 32(b), 32(c), and 32(d)* outline the parameters for computing these amounts, which vary by earned income/adjusted gross income, filing status, and family size.

    - The earned income amount works much like the current law EITC. The amount is based on a percentage of earnings that will phase in at varying rates depending on filing status and then phase out at a rate of 5 percent once earned income or adjusted gross income (AGI) exceeds a set amount, again depending on filing status. The earned income amount will phase out completely before the taxpayer becomes liable for the individual income tax.

    - The child benefit amount is meant generally to replace the CTC and ACTC. The child benefit amount is phased in with earnings at a 15 percent rate; it would be capped at a maximum amount of $1,590 per child; and it would phase out with earned income or AGI at $75,000 or $110,000 for married filing jointly taxpayers at a rate of 5 percent.

    - Finally, the additional child benefit amount is meant to replace the EITC for children. Like the current EITC for children, the additional child benefit amount phases in as a percentage of earnings at a rate that depends the number of children and then phases out once earned income or AGI exceeds a certain amount.

The rates and amounts related to earned income amount and the additional child benefit amount are as follows:

Earned income amount

Single filer				Joint filers				Head of Household filers			
Earnings	Base Rebate	Phase in Rate	Phase out Rate	Earnings	Base Rebate	Phase in Rate	Phase out Rate	Earnings	Base Rebate	Phase in Rate	Phase out Rate
0	0	25.1%	0%	0	0	25.1%	0%	0	0	25.1%	0%
6,100	1,530	17.1%	0%	12,200	3,059	17.1%	0%	9,150	2,294	17.1%	0%
9,000	2,025	0%	5%	18,000	4,049	0%	5%	13,500	3,037	0%	5%
49,494	0	0%	0%	98,988	0	0%	0%	74,241	0	0%	0%

Additional child benefit amount

One Child				Two Children				Three or More Children			
Earnings or AGI	Base Rebate	Phase in Rate	Phase out Rate	Earnings or AGI	Base Rebate	Phase in Rate	Phase out Rate	Earnings or AGI	Base Rebate	Phase in Rate	Phase out Rate
0	0	11%	0%	0	0	17%	0%	0	0	19%	0%
20,000	2,200	0%	0%	20,000	3,400	0%	0%	20,000	3,800	0%	0%
25,000	2,200	0%	15%	25,000	3,400	0%	15%	25,000	3,800	0%	15%
39,667	0	0%	0%	47,667	0	0%	0%	50,333	0	0%	0%

- *Section 32(e)* defines "eligible taxpayer." An eligible taxpayer must live in the United States for more than one-half of his or her taxable year and must not be another taxpayer's dependent. In addition:

  - An eligible taxpayer may not be another taxpayer's qualifying child.

  - An eligible taxpayer cannot have claimed the benefits of current Internal Revenue Code section 911 (relating to certain elections made by citizens or residents of the United States living abroad).

  - Nonresident alien individuals are not eligible taxpayers unless they are treated as a resident of the United States by reason of an election under Internal Revenue Code section 6103.

  - Finally, no rebate is allowed unless an eligible taxpayer provides individual taxpayer identification numbers for himself or herself, his or her spouse (if applicable), and each qualifying child (if applicable). Special rules are provided to ensure fair treatment of military personnel stationed outside of the United States.

- *Section 32(f)* defines qualifying child in reference to Internal Revenue Code section 152(c).

- *Section 32(g)* defines "earned income" to include wages, salaries, tips, and earnings from self-employment. Income received from pensions and annuities, income of non-resident alien individuals that is not connected with the United States, amounts received for services provided by inmates at penal institutions, and certain subsidized work activities under the Social Security Act are not taken into account. A taxpayer may elect to include combat zone pay under current Internal Revenue Code section 112 as earned income.

  "Earned income" does not include federal government cash transfers such as Social Security and Supplement Security Income benefits. Major government cash transfer payments are adjusted using the Consumer Price Index (CPI); typically, the CPI-W (for urban wage earners and clerical workers) or CPI-U (for all urban consumers). Both of these indexes currently include taxes (such as sales and excise taxes) that are directly associated with the price of goods and services. Thus, the adjustment already associated with these programs should reflect any change in the price of goods due to the PCT. For example, households that receive Social Security benefits would see an increase in those benefits that accounts for the PCT.

- *Section 32(h)* only allows a rebate in the case of a taxable year that is a full taxable year (a period of 12 months), except in the case of the death of a taxpayer.

- *Section 32(i)* provides that the rebate amount will not be counted as income for certain means-tested programs.

- *Section 32(j)* requires the Secretary to determine the amount of the rebate under tables (an administratively simpler way for taxpayers to determine their rebate amount).

- As under the current earned income tax credit, *Section 32(k)* denies the rebate if a taxpayer has a certain amount of disqualified income. For this version of the Progressive Consumption Tax Act, that amount is set at $5,000. "Disqualified income" means investment income like interest or dividends, tax-exempt interest, rents or royalties not derived in the ordinary course of a trade or business, capital gain net income, and net income from passive activities (defined under current Internal Revenue Code section 469).

As with the earned income tax credit, the intent of the disqualified income provision is to exclude taxpayers who have little earned income, but are nonetheless high-income taxpayers, from receiving the rebate. However, this intent must be balanced with the fact that many older Americans in particular may depend on some of these disqualified income sources. Thus, the $5,000 limit is informed by recent AARP data on the total income sources for Americans aged 65 or older. According to that data, which was compiled in 2012, the median interest, dividend, and rental income for Americans over 65 in the highest income quintile (the top 20%) was $3,454.

- *Section 32(l)* adjusts the earned income amount, child benefit amount, and additional child benefit amount to inflation.

- *Section 32(m)* provides restrictions on taxpayers who improperly claimed the rebate in the prior taxable year. These provisions are identical to those under current Internal Revenue Code section 32.

Section 206(b) provides conforming amendments.

Under Section 206(c), the comprehensive rebate provisions apply to taxable years beginning after December 31, 2017.

Other technical and conforming amendments

Section 207. Section 6 directs the Secretary of the Treasury to produce other technical and conforming changes necessary to reflect the changes in Subtitle A.

Subtitle B. Subtitle B reduces the corporate income tax rate.

Section 211. Section 211, the only section in Subtitle B, lowers the corporate income tax rate to 17 percent. The amendments made by Section 211 apply to taxable years beginning after December 31, 2017.

TITLE III: REFUND OF EXCESS PROGRESSIVE CONSUMPTION TAX REVENUE

One goal of PCT-based reform is to more reliably raise the revenues that we need to for real investments that benefit all taxpayers—such as investments in defense, health, education, and infrastructure programs.

However, the PCT is not meant to be a means to quickly raise revenues while disregarding the effects of higher consumption taxes on U.S. families and employers. Thus, Section 4 of the Progressive Consumption Tax Act includes a revenue "circuit breaker" mechanism to address these concerns and to benefit taxpayers.

Section 301(a) adds a new Section 6433 to the Internal Revenue Code that provides for a refund of excess progressive consumption tax revenue.

- *Section 6433(a)* provides that "eligible filers" may receive a "consumption tax refund amount" in any "qualifying excess consumption tax revenue year."

- *Section 6433(b)* defines "qualifying excess consumption tax revenue year" as any calendar year for which net consumption tax revenues exceed 10 percent of gross domestic product (GDP) for that year. "Net consumption tax revenue" means the amount of PCT collected under new section 3901 minus any credits allowable under new section 3916. Calendar-year GDP is estimated by the Department of Commerce.

- *Section 6433(c)* defines "eligible filer" to include any individual who, with respect to the qualifying excess consumption tax year, has filed an income tax return (which includes those who do not have an income tax liability but who have filed for a PCT rebate). However, "eligible filer" does not include nonresident aliens, individuals that have been claimed as dependents, or estates and trusts. A non-calendar year taxpayer's taxable year must overlap by at least six months with the excess consumption tax revenue year for that taxpayer to qualify to receive a refund of the excess consumption tax revenue.

- *Section 6433(d)* outlines how the consumption tax refund amount is computed. In formula form:

  Excess consumption tax revenue = x*(eligible filer, non-joint return) +
  2x*(eligible filer, joint return) + 0.5x*(qualifying children)

  Thus, each eligible filer receive one "share" of the excess consumption tax revenue; joint filers receive two shares; and filers with qualifying children receive additional one-half shares. The ultimate amount of each share depends on the amount of excess consumption tax revenue.

- *Section 6433(e)* indicates that excess consumption tax revenue payments should be made a soon as practicable.

Section 301(b) contains conforming amendments.

Section 301(c) provides that the amendments made by Section 301 take effect as of the effective date of the Progressive Consumption Tax Act.